

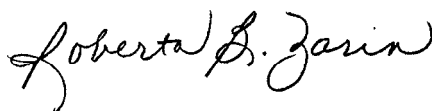
## PREFACE

Exempt Organizations (EO) is dedicated to fulfilling the IRS mission to help all customers understand and meet their tax responsibilities. Customer Education & Outreach (CE&O) works closely with Exempt Organizations staff to accomplish this by:

- Developing tailored education programs for customer sub-segments,
- Coordinating the development, revision and design of forms, publications and other non-speaker outreach activities,
- Making standardized educational materials available for outreach efforts, and
- Establishing a means for customers to be heard.

This workshop and our materials are part of a tailored program for representatives of small and mid-sized exempt organizations. We hope that this text helps you become more familiar with tax laws governing exempt organizations and understand how compliance with these laws will strengthen your organization.

The material in this book is for educational use only and may not be cited as precedent.



Roberta “Bobby” Zarin  
Director, Customer Education and  
Outreach, Exempt Organizations

## Exempt Organizations Workshop

---

<b>Objective</b>	<p>Upon completion of this text you will know what an organization exempt under section 501(c) of the Internal Revenue Code must do to:</p> <ul style="list-style-type: none"><li>• Report your organization's UBI appropriately; and</li><li>• Conduct charitable gaming lawfully, and withhold and report gaming taxes appropriately.</li></ul>
<b>Please Note</b>	<p>The material in this text is for educational use only in association with the Exempt Organizations Workshop. It is not intended to establish Internal Revenue Service positions and may <u>not</u> be relied upon or cited as precedent.</p>
<b>For More Information</b>	<p>This text primarily focuses on requirements for 501(c)(3) organizations. Some basic information is presented about organizations exempt under other code sections as well. For a more detailed discussion, including exceptions to the general information provided in this text, please refer to the publications and sections of law cited in the material. Each chapter of this text contains a complete list of references.</p>
<b>Legal Authority</b>	<p>The Internal Revenue Code appears as Title 26 of the United States Code. Congress originally enacted the Internal Revenue Code on August 16, 1954, as the Internal Revenue Code of 1954. It was comprehensively updated when Congress passed the Internal Revenue Act of 1986 on October 22, 1986. Both of these original laws have been amended numerous times by Congress. The resulting body of law guides all tax administration in the United States.</p> <p>The IRS issues regulations that set forth its interpretation of the law. The regulations are issued over the signature of the Secretary of the Treasury (or his delegate) under Title 26 of the Code of Federal Regulations. The regulations carry more weight than any rulings or releases on tax matters otherwise issued by IRS or the Treasury.</p>
<b>Internal Revenue Code (IRC) Citations</b>	<p>All references are to the Internal Revenue Code (IRC) unless otherwise stated. For example, “section 501(c)(3)” refers to Internal Revenue Code section 501(c)(3). The Internal Revenue Code is also sometimes referred to as simply “the Code”.</p>

## CHAPTER 5

### GAMING ACTIVITIES

---

#### Gaming as a Fundraising Activity

Many exempt organizations commonly and successfully use gaming activities to raise funds for their programs.

Organizations that conduct or sponsor gaming activities, whether for one night or throughout the year and whether in their primary place of operations or at a remote location, are subject to federal tax law requirements and must be aware of the rules governing income, employment, and excise taxes.

The term *gaming* includes activities such as bingo, Beano, raffles, lotteries, “instant” bingo, pull-tabs, scratch-offs, pari-mutuel betting, Calcutta wagering, pickle jars, punchboards, tip boards, tip jars, and certain video games.

---

#### Gaming and Unrelated Business Income Tax

Generally, unless an exception applies, unrelated business income tax (UBIT) is paid on receipts derived from gaming. Income from bingo is excluded from the unrelated business income tax by the Code (see Chapter 4), as is income from lawful gaming conducted in North Dakota.

Lawful gaming ordinarily requires a license from the state in which the gaming is conducted.

---

#### Gaming Activities and 501(c)(3) Organizations

Gaming is generally a business activity that does not further section 501(c)(3) purposes. Thus, a section 501(c)(3) organization may conduct gaming only if the gaming is not a substantial part of the organization’s activities and if it provides funds for the organization’s exempt purposes.

---

#### Wagering Taxes

There are two taxes relating to wagering. One is an excise tax on certain wagering transactions. The other is an occupational tax on persons who make a business of accepting wagers. A person liable for the excise tax on wagering is automatically liable for the occupational tax on wagering and must register the wagering activity with the IRS.

---

## GAMING ACTIVITIES, Continued

---

### Definition of Wager

For purposes of the tax, ‘wager’ means any wager with respect to a sports event or a contest, any wager placed in a wagering pool conducted for profit with respect to a sports event or a contest, and any wager placed in lottery conducted for profit.

*Conducted for Profit:* A wagering pool or lottery is conducted for profit not only if it earns a direct profit but also if it is expected to generate increased sales or attendance, or if the operator takes a percentage of the contributions or charges a fee to join the pool.

---

### Wagering Excise Tax

The taxes on wagering apply to wagers placed in a lottery conducted for profit (i.e., for the purpose of raising funds). Pull-tabs, raffles, and tip jars meet the definition of taxable wagers placed in a lottery.

The wagering tax applies to the sum risked by the person placing the bet, not the amount the person stands to win.

---

### Wagers Exempt From Wagering Tax

There is no wagering tax on amounts paid to play a coin-operated device. In addition, there is no wagering tax on wagers placed on the following:

#### **(a) Games When All Are Present**

A wager placed in a game in which the wagers are placed, the winners are determined, and the prizes are distributed in the presence of all persons placing wagers in such game is not subject to the wagering tax.

Games of this type involve “group play” and include bingo, keno, card games, dice games, and games involving wheels of chance, such as roulette wheels.

#### **(b) Drawings Conducted By Exempt Organizations**

A wager placed in a drawing conducted by a tax-exempt organization is not subject to the tax on wagers, so long as no part of the net proceeds from such drawing *inures to the benefit of any private shareholder or individual*.

*Drawing:* A drawing is any physical drawing of a ticket or use of a wheel or similar device by which the winner is conclusively determined by a number, letter, legend, or symbol without reference to outside event that is beyond the control of the operator.

---

## GAMING ACTIVITIES, Continued

---

### **Wagers Exempt From Wagering Tax** (continued)

*Inures to the Benefit of Private Shareholders or Individuals:* The proceeds of a drawing are said to inure to the benefit of private shareholders or individuals when, for example, the expenses of the drawing, including the salary of the operator, are unreasonable. When the drawing is conducted by a membership organization, such as a social club, fraternal society, or veteran's organization, the proceeds of drawings that are limited to members are not deemed to inure to the private benefit of the members if the proceeds are used for the operation of the club or society. However proceeds, all or part of which come from nonmembers, are deemed to inure to members if used to reduce membership dues or to pay costs that would normally be paid from member dues or assessments. And, proceeds of drawings that are open to the public inure to the benefit of members if such proceeds help to defray the organization's expenses.

### **(c) Coin-Operated Device**

The wagering tax is not assessed on amounts spent to operate *coin-operated devices*. Coin-operated devices include slot machines, pinball machines, and machines that display poker hands.

---

### **How is This Tax Determined?**

The wagering excise tax applies to the gross amount of wagers received. This means that the tax is based on the total amount received before any payout of prizes or other expenses. The tax rate is determined by whether the wager is authorized under the laws of the state in which it is accepted. If the wager is authorized, the rate of tax is 0.25 percent of the amount of the wager. If the wager is not authorized, the tax is 2 percent of the amount of the wager.

---

## GAMING ACTIVITIES, Continued

---

Form 730,  
*Monthly Tax on  
Wagers*

The organization reports and pays the wagering excise tax by filing Form 730, *Monthly Tax on Wagering*. It is due each month by the last day of the month after the month in which the wager was placed. If an organization accepts taxable wagers, it should file a return for each month regardless of whether or not it has taxable wagers to report for that month. If it has none to report, it should write “0” (zero) in the last box of the dollar amount. If it stops accepting wagers, it should check the final return box above Line 1. An organization may be subject to a penalty for failure to file the form and for failure to pay the tax.

---

Record-  
Keeping for  
Wagering Tax

Every person liable for wagering tax must keep a daily record showing the gross amount of all wagers on which a tax is due. Among other things, the daily records must show:

- The gross amount of wagers accepted, and
  - The gross amount of each class or type of wager accepted on each separate event, contest, or other wagering medium.
- 

Occupational  
Tax

The Code also imposes an occupational or stamp tax in connection with certain wagers. This tax is an annual fee imposed on both the organization and each of its employees who receive wagers.

The amount of the occupational tax depends on whether the wager is authorized under the laws of the state in which the wager is accepted. If the wager is authorized, the amount of the tax is \$50 per year per person. If the wager is not authorized, the amount of the tax is \$500 per year per person.

---

Form 11C,  
*Occupational  
Tax and  
Registration  
Return for  
Wagering*

An organization reports and pays the occupational tax on wagering with Form 11C, *Occupational Tax and Registration Return for Wagering*. Form 11C must be filed before an organization begins accepting wagers. After that, the organization must file a renewal return by July 1 for each year in which the organization accepts wagers. A Form 11C should also be filed when certain changes in ownership occur, while a supplemental registration return should be filed when certain other changes occur. An organization may be subject to a penalty for failure to file the form and for failure to pay the tax.

---

## GAMING ACTIVITIES, Continued

---

Examples of  
Excise and  
Occupational  
Tax  
Applicability

Example: An exempt organization conducts a raffle open to the general public. The organization deposits all of the proceeds into its scholarship fund for local college students from which it awards an annual scholarship in furtherance of exempt purposes. Because the organization does not use any of the raffle's proceeds for administrative expenses or to benefit a private individual, the raffle does not meet the definition of a taxable wager. Therefore, no wagering taxes apply.

Example: An exempt organization sells pull-tabs at its building. The organization uses some proceeds to pay its real estate taxes. The organization has four employees selling pull-tabs. This organization would be liable for the wagering excise tax because it used a portion of the proceeds from its pull-tab sales to pay for its operational expenses. Because the excise tax applies, the organization and its four pull-tab sellers would be required to file the annual occupational tax.

---

Form W-2G,  
Certain  
Gambling  
Winnings

An exempt organization that conducts gaming must report to the IRS certain gambling winnings and any federal income tax that it is required to withhold on those winnings.

---

Which Winnings  
Must an  
Organization  
Report?

In general, the organization must report gambling winnings that are \$600 or more and that are at least 300 times the amount of the wager. The organization has the option of deducting the cost of the wager from the winnings in determining whether the \$600 threshold is met.

Example: An organization conducts pull-tab games. Mr. G buys a \$2 pull-tab and wins \$10,000. Because the amount won is greater than \$600 and is 5000 times the amount of the wager, the organization must report Mr. G's winnings.

Example: Mr. S buys a \$2 pull-tab and wins \$600. You may reduce the amount of the winnings by the cost of the wager, in which case the winnings are \$598. You do not have to report the winnings because the \$600 threshold is not met.

---

## GAMING ACTIVITIES, Continued

---

Keno Games      An organization conducting keno games must report keno game winnings that are \$1,500 or more after deducting the cost of the wager.

*Example:* Ms. E wagers \$5 on keno at an exempt organization and wins \$1,500. Because the winnings are less than \$1,500 after deducting the cost of the wager, the organization does not have to report the winnings.

---

Bingo Games and Slot Machines      Exempt organizations must report winnings at a bingo game or slot machine that are \$1,200 or more before deducting the cost of the wager.

---

When to File Form W-2G      An exempt organization reports gambling winnings by filing a Form W-2G for every person to whom it pays the winnings.

*Multiple Winners:* When the person receiving gambling winnings is not the actual winner or is one of a group of two or more winners, he or she must complete Form 5754, *Statement by Person(s) Receiving Gambling Winnings*, and give it to the organization. Form 5754 is used to provide information about each winner and each winner's share of the winnings. An organization then prepares a Form W-2G for each of the persons listed as winners on the Form 5754.

If an organization files on paper, it must file copy A of Form W-2G by February 28 following the calendar year in which it pays the winnings. Use Form 1096 to transmit paper Forms W-2G. If it files electronically, it must file Form W-2G by March 31 following the calendar year in which it pays the winnings. If it is required to file 250 or more Forms W-2G in a year, it must file them electronically.

In addition, an organization must give copies B and C of Form W-2G to the winner by January 31 following the calendar year in which it pays the winnings.

---



## GAMING ACTIVITIES, Continued

---

### Income Tax Withholding from Gaming Winnings - Regular Withholding

An organization that conducts gaming must withhold income tax from certain gambling winnings. The proceeds of gambling winnings greater than \$5,000 are subject to withholding at a rate of 25 percent if won in the following:

- A wager placed in a sweepstake, wagering pool, or lottery, and
- Any other wagering transaction, if the amount of the proceeds is at least 300 times as large as the amount wagered.

The total proceeds from the wager are subject to withholding, not just the amounts in excess of \$5,000.

If the winnings are in the form of a noncash payment, such as a car, the fair market value of the item won is considered the amount of the winnings. An organization must withhold income tax if the fair market value of the item won exceeds \$5,000 after deducting the price of the wager. The amount to withhold depends on the organization or the winner pays the withholding tax:

- If the winner pays the withholding tax to the organization, it must withhold 25 percent of the fair market value of the item won minus the amount of the wager,
  - If the organization pays the withholding tax, it must withhold 33.33 percent of the fair market value of the item won minus the amount of the wager.
- 
-

## GAMING ACTIVITIES, Continued

---

### Exception to Regular Withholding

Generally, organizations do not withhold income tax on winnings from slot machines, keno, or bingo, unless they are required to “backup withhold.”

Each person who receives a payment of winnings subject to withholding must provide the organization with a statement on Form W-2G containing:

- His or her name, address, and taxpayer identification number, and
  - A declaration that no other person is entitled to any portion of the payment.
- 

### Backup Withholding from Gaming Winnings

If an organization is required to report winnings on Form W-2G, the winner is supposed to provide his or her name, address, and taxpayer identification number so that the preparer can properly complete the form. If the winner does not provide this information and if the winnings were not subject to 25 percent regular withholding, the organization must withhold income tax at the backup withholding rate of 28 percent.

---

### Reporting the Withholding on Form 945

The organization is responsible for paying regular or backup withholding, whether or not it collects the withholding from the prize recipient. The best time to collect withholding or backup withholding is before the prize is paid.

An organization reports regular and backup withholding from gaming winnings on Form 945, *Annual Return of Withheld Federal Income Tax*. Form 945 is an annual return and is due by January 31 of the year after the year in which the taxes were withheld.

---

### Additional Examples of Reporting and Withholding

*Example:* ABC Charity conducts a raffle in which it sells tickets for \$25 each. The grand prize is \$6,000 in cash. Form W-2G is required because withholding is required for raffle proceeds that exceed \$5,000. Withholding on raffle prizes is not affected by the ratio of the prize to the wager. Because the prize less the price of the ticket is \$5,975 ( $\$6,000 - \$25 = \$5,975$ ), the withholding would be \$1,494 ( $\$5,975 \times 25$  percent).

---

## GAMING ACTIVITIES, Continued

---

### Additional Examples of Reporting and Withholding (continued)

Example: Nonprofit Charity conducts a fundraising event in which it sells raffle tickets for \$2 each. The prize is a large screen TV with a fair market value of \$2,000. Because the prize less the value of the ticket is \$600 or more and greater than 300 times the amount of the wager, the organization must complete form W-2G, but does not have to withhold because the prize is less than \$5,000.

Example: CDN, an exempt organization, has a winner of \$5,100 from one of the pull-tabs, which cost \$10. Because the winnings, less the wager, exceed \$5,000, Form W-2G is completed and federal income tax is withheld. Income tax withheld is reported on Form 945. The winner would receive \$3,827 (\$5,100 gross winnings less \$1,273 withholding tax) (computed (\$5,100 - \$10) x 25 percent).

Example: CDN, an exempt organization, conducts a weekly bingo game. A payout of \$1,300 is made for a single game. The winner furnishes identifying information, along with her SSN, to the organization. The organization must complete Form W-2G because the winnings exceed \$1,200. The regular gambling withholding of 25 percent does not apply to bingo.

Example: XYZ Charity conducts a raffle in which it sells tickets for \$10 each. The grand prize is a snowmobile with a fair market value of \$7,000. As explained in the first example, the winnings are subject to regular gambling withholding and Form W-2G is required.

---

### Failure to File Correct Information Returns by the Due Date

If an organization does not file a correct information return (Form 945 *Annual Return of Withheld Federal Income Tax*) by the due date and cannot show reasonable cause, it may be subject to a penalty. The penalty applies in cases of failure to file timely, failure to include all information required to be shown on a return, or inclusion of incorrect information on the return. The penalty is generally \$50 per document unless correction is made within certain time frames.

---

## GAMING ACTIVITIES, Continued

---

Failure to  
Furnish Correct  
Payee  
Statements

If an organization fails to provide correct payee statements (Form W2-G *Statement for Recipients of Certain Gambling Winnings*) and cannot show reasonable cause, it may be subject to a penalty. The penalty applies for failure to provide the statement by January 31, failure to include all information required to be shown on the statement, or failure to include correct information on the statement. The penalty is \$50 per statement, regardless of when correct statement is furnished, with a maximum of \$100,000 per year.

---

For More  
Information

Publication 3079, *Gaming Publication for Tax-Exempt Organizations*

Form 730, *Monthly Tax on Wagering*, and Instructions

Form 11C, *Occupational Tax and Registration Return for Wagering*, and Instructions

Form W-2G, *Statement for Recipients of Certain Gambling Winnings*

Form 945, *Annual Return of Withheld Federal Income Tax*

---

Forms and  
Publications

You may order Forms and Publications by calling (800) 829-3676 or by downloading them from [www.irs.gov/](http://www.irs.gov/).

---

## CLOSING

---

### Exempt Organizations and the Internal Revenue Service

The goal of the Exempt Organizations office of the IRS is to promote compliance with the tax laws governing exempt organizations. It does this:

- Through outreach and educational efforts
  - By issuing rulings that apply tax laws to an exempt organization's specific set of facts
  - Through examinations and other compliance activities
- 

### Ways Exempt Organizations Can Get Help from the IRS

The IRS has several ways that officers or representatives of exempt organizations can get help on tax issues:

Customer Account Services: Call (877) 829-5500 (toll free). Ask Exempt Organizations specialists general questions about exempt organizations or questions about a specific organization's account. The caller must have the organization's employer identification number (EIN) handy and know the organization's legal name.

For some account-specific questions, the caller will need to establish his or her right to access the information. He or she must be an authorized officer or a representative of the organization with power-of-attorney rights.

EO Website: Point your browser to [www.irs.gov/eo](http://www.irs.gov/eo) for a wealth of information and "how-to" assistance including:

- Descriptions, rules, and requirements for different types of exempt organizations
  - Life Cycle of an Exempt Organization
  - Published guidance
  - Tips on how to avoid filing errors
-

## CLOSING, Continued

---

More Ways  
Exempt  
Organizations  
Can Get Help  
from the IRS

Web-based Training. Go to [www.stayexempt.irs.gov](http://www.stayexempt.irs.gov) to participate in a “virtual” workshop or to view on-line “mini-courses” on a variety of EO topics.

Forms and Publications: Call (800) 829-3676 to order free IRS publications and forms or download them from the IRS website at [www.irs.gov/](http://www.irs.gov/).

---

For More  
Information

General IRS Questions: (800) 829-1040 (toll-free)

TEGE Customer Service: (877) 829-5500 (toll-free)  
(EO questions)

Forms and Publications: (800) 829-3676 (toll-free)

IRS Internet Site: [www.irs.gov](http://www.irs.gov)

EO Page: [www.irs.gov/eo](http://www.irs.gov/eo)

On-line Training: [www.stayexempt.irs.org](http://www.stayexempt.irs.org)

EO Update: Subscribe to this IRS e-mail service to receive the following related to exempt organizations: news releases, new forms, guidance and other publications, changes and additions to the EO Page on IRS.gov and information about upcoming training and outreach events. Visit [www.irs.gov/eo](http://www.irs.gov/eo) to subscribe.

---

The IRS Needs  
YOUR Help

The IRS would like your feedback on our products. Please contact us with your recommendations on changes or additions that would improve your understanding of exempt status requirements.